

THE ART OF POSITIONING

bancography

BRANCH PRODUCT RESEARCH BRAND

Some consumers continue to prefer cash for its speed at the point of purchase, ubiquitous acceptance and anonymity.

Building an ATM Deployment Strategy

After several decades of continual growth, the total volume of ATM transactions in the U.S. has leveled off in recent years. Though not declining in aggregate, ATM transactions have remained constant while the nation's household base has grown, indicating a decline in per capita usage. The ATM has been challenged by several alternatives. Cash back from point of sale registers is now prevalent at grocery and drug stores and numerous other retailers. Debit cards have replaced cash as a primary payment vehicle for several consumer segments. And online and ACH payments have reduced the cash needs of many consumers.

Yet some consumers continue to prefer cash for its speed at the point of purchase, ubiquitous acceptance and anonymity – with the lattermost perhaps increasing in importance as news reports of compromised account numbers heighten privacy and security fears. Many merchants favor cash, too, which carries neither the interchange fees of card payments nor the loss risk of checks. Further, while ATM availability is rarely cited as a primary driver of institution choice, it is frequently cited as a cause of attrition by surcharge-weary customers lacking convenient ATMs from their own institution.

Thus, an offsite ATM network remains an important supplement to the branch channel for many institutions, especially those that target the entry and mass market segments. However, given the costs of deployment and servicing, it can prove difficult to build

a profitable offsite ATM network. A successful ATM network requires an underlying strategy, and there are four primary approaches to offsite ATM deployment.

Branch forerunner:

ATMs are used in submarkets targeted for future branching to provide service until a branch opens, increase brand awareness and serve customers in adjoining submarkets. This approach is most effective in high growth markets where the institution owns a small network, and demographics indicate a high propensity for ATM use. Branch forerunner ATMs do not always realize profitable transaction volumes, but they contribute value by building awareness of the institution in advance of branch construction.

Offload capacity and extend branch network reach:

ATMs are used in areas where the institution enjoys dense customer bases to relieve branch congestion and provide convenience. This approach is especially important in mature markets, where retention is paramount. ATMs that are deployed with an objective of improving service to current customers in high penetration markets may not prove profitable on surcharge and interchange fees. However, the opportunity value of transactions removed from the higher cost branch channel and the increase in retention rates from improved convenience can justify these deployments. *(continued on page two)*

Is Your Check Brand Light On?

Sputtering. Hesitation. Inefficiency. Loss of power. All are symptoms of an automobile engine when it needs a tune-up. Sometimes you sense it, sometimes you feel it. Most often the *Check Engine* warning light appears, but you have no idea what it means or what to do about it until you take the car to your mechanic. And sadly, many people ignore the warning

light until the symptom becomes severe enough to warrant immediate and sometimes costly attention.

Maintaining your institution's brand sometimes follows the same path. There are signals that indicate something is amiss or not synced up correctly. These signals can be subtle and easy to miss. Or, just like the *Check Engine* light, they can be ignored. But that never turns out well – for your car or your brand.

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A successful ATM network requires an underlying strategy.

Building an ATM Deployment Strategy *continued from page one*

Fee income:

ATMs are deployed in high traffic areas where price-inelastic consumers will pay fees for immediate cash (malls, airports, casinos, stadiums, etc.). Though most effective in a market where the institution maintains a consumer oriented network (since the continual fees may encourage non-customers to move their relationships), the strategy can thrive in any venue with sufficient transaction volumes. The strategy carries risks, in that lease rates for premium locations are high, lease terms can be long and non-bank providers (i.e., the independent service organizations) often enjoy a cost advantage in bidding due to less stringent internal security policies. Further, because the rationale for this approach is driven by revenue from non-customers, the strategy does little to build the institution's core relationship base and may be viewed by management as a peripheral business line.

Branding:

ATMs are deployed in partnership with third party providers, usually in bulk installations in retail stores, convenience stores, hotels or other abundant but typically low volume venues. The partnerships are at best revenue neutral, in that the third party owns the machines but the bank or credit union contributes

a small fee and provides signage in exchange for which its customers receive fee-free transactions. The terminal owner benefits from the arrangement due to both the fee from the bank or credit union and from the credibility that a bank-branded ATM provides. For limited capital outlay, the partnerships can establish presence in underserved markets and provide a convenient means for current customers to obtain cash fee-free. However, because the institution does not share in the foreign revenue stream, these are by definition marketing expenses with no overt profit implications.

While institutions can pursue more than one of the strategic options, it is beneficial to define expectations for the ATM network in the context of those options before investing in machines and leases, as each carries different customer service and profit implications. The institution seeking to expand its footprint might choose the branch forerunner or branding options; but the institution seeking new non-interest income streams would choose the mall/airport/casino option; while a market leader confronting severe branch congestion would favor the offload capacity option. Regardless of which strategy is pursued, the presence of predetermined goals for the ATM channel can yield a more focused, cohesive network.

Bancography, After 10 Years

On July 16, 2001, we launched Bancography with a goal of bringing analytic sophistication, industry research and education to the marketing and delivery efforts of financial institutions of all sizes. That we started a company with a specific focus on branch distribution planning in advance of the largest branch construction boom in U.S. history was likely more serendipitous than prescient. Nonetheless, by the middle of the decade, as one of our business banker colleagues described it, we'd completed the transition from startup to small business. Since then, we've seen one of the most troubled times in our industry's history, including numerous bank failures and industry-wide earnings pressure.

Against that backdrop, we appreciate the loyalty our clients and colleagues have shown us over these 10 years all the more. To those who have been with us since the early days, thank you for your trust; you helped build our company. To those who have joined us more recently, thank you for your confidence; we'll strive to justify your choice. And to those who read our *Bancology* journal and attend our online Bancography Briefings but are not clients, please continue to join the conversation with us.

We welcome the dialogue across the industry. In the years ahead we will continue to deliver superior research and analytics, theoretically grounded but applied in the context of each market's competitive realities. We have enjoyed and appreciated these 10 years tremendously, both the analytics and the relationships we've developed. Thank you to all our readers for your support and interest!



Branch Profitability: Deconstructing the Branch Income Statement

In its simplest construct, profitability is a function of two elements: revenue and expenses. In banking, much attention is given to the revenue side of the income statement in the form of sales management efforts to boost balances and product management efforts to increase margin and non-interest revenues. However, in mature markets, small rural markets or overly competitive markets, revenue growth can prove difficult to attain, leaving the expense side of the income statement as the primary means to impact branch profitability. This article will discuss the key components of the expense side of the branch income statement.

In most branches, **salaries and benefits** represent about two-thirds of total non-interest expenses. As such, staffing represents the area where a branch manager can most directly impact the expense side of the income statement. With acceptance of new payment technologies continuing to increase, staffing optimization involves more than simply aligning branch resources with demand. Banks and credit unions

should actively educate consumers on alternatives to traditional low value teller transactions. For example, image-enabled ATMs can remove deposit transactions from the teller workload, but acceptance can be slow unless the branch staff teach the customers to use the new technology.

Occupancy costs are rarely within the direct control of the branch, having usually been determined by corporate management when the branch was initially built or leased. Further, for owned properties, much of the occupancy expense is impounded in depreciation, a non-cash charge. Thus, when examining branch profitability for the purpose of evaluating a branch manager's performance, be sure to remove occupancy costs that are beyond that officer's control.

Miscellaneous direct operating expenses include office supplies, subscriptions, telecommunications, postage, local advertising and community contributions. Regarding the final two elements, at many institutions branch

managers have discretion over small investments, with a maximum authority usually in the \$500 range. All in, miscellaneous direct expenses should not exceed \$3,000 per month for a branch with a moderate-sized deposit base.

Reporting structures vary across institutions, including whether **direct processing expenses** appear on a general ledger branch income statement. These expenses rightfully should be charged to the branch, since the branch receives all credit for the margin and fee income its products generate. The expenses directly related to that income stream (e.g., statement rendering and postage, debit card production) therefore should appear among the branch expenses if possible.

In contrast, **corporate overhead**, including executive salaries and operations and technology costs, remains mostly fixed, supports more than just the branch based lines of business and is only loosely related to the size of any individual branch's portfolio. Accordingly, these expenses should be omitted from the branch income statement.

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Is Your Check Brand Light On? *continued from page one*

Not many people would trade their car for another one because the *Check Engine* light was on. A tune-up by a qualified repair shop should enable your vehicle to return to its previous efficient and smooth running condition. Your institution's brand can be handled the same way by seeking a qualified brand development organization to review and adjust it.

In some cases at Bancography, institutions have asked us to develop a new brand for them when it was not necessary. Several institutions presented solid brands with interesting heritage and strong brand equity, but the brands had lost their way. The institutions' lack of focus, consistency and continuity with their brand communications resulted in a loss of power. Just like the out-of-tune auto.

Most often, the brand loses the ability to express its differentiation. Not having a clear,

concise and easy-to-understand brand position results in being lost in the sea of sameness from all the other competitors operating in the same space. The building blocks of differentiation are there, they've just been forgotten, ignored or misfired. The brand needs a tune-up.

Bancography's Brand Tune-up service returns your brand to its high efficiency mode. It examines your marketing communications and the total customer experience you deliver to determine if your brand is standing apart from the crowd. Is your brand

promise clear? Messages consistent? Personality evident? Tonality correct? Imagery appropriate? Can all your associates express how your institution is different in a few short but concise words?

Any of these checkpoints (and others) can throw your brand out of tune. Any of them can cause your *Check Brand* light to illuminate.

The question is, do you see it? Or worse, are you ignoring it?

Don't delay any longer. Ask Bancography's qualified brand mechanic John Mathes to inspect your brand. He's been tuning financial brands for a long time and can deliver an affordable and executable plan to return your brand to its most efficient state.

Contact John at john@bancography.com or (770) 360-5710.



Finally, it can be beneficial to include some ***adjustment for transactions that the branch performs on behalf of customers booked at other branches***, since the branch is incurring the salary cost to process the transaction but receiving none of the margin and fee income from that account. This adjustment can take the form of a credit to staff expense or as an adjustment to margin and fee income. Of course, it can be positive or negative depending on whether the branch is a net

processor or net supplier of other-branch transactions. Few institutions operate core systems that can support this type of adjustment, but there are several methods for calculating an appropriate adjustment, which must be zero-sum across the institution overall (i.e., amounts debited from one branch must be equally credited at others). The specific details and pros and cons of these methods remain beyond the scope of this article, but please contact us if you would like to review options for calculating transaction adjustments at your institution.

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a Quarterly Journal from Bancography***